

**WRITTEN TESTIMONY OF  
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INTERNAL REVENUE SERVICE  
BEFORE THE  
HOUSE WAYS AND MEANS COMMITTEE  
IRS IMPLEMENTATION OF TAX-RELATED PROVISIONS IN THE AFFORDABLE  
CARE ACT  
ON  
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**Introduction**

Chairman Camp, Ranking Member Levin, and Members of the Committee, thank you for the opportunity to appear before you today to discuss the work the IRS has been doing to fulfill our responsibilities under the Affordable Care Act (ACA).

The IRS is charged with implementing the tax-related provisions of the ACA. Our most substantial implementation effort in this regard involves the delivery of premium tax credits that will help millions of American families afford health insurance starting in 2014, when the new Health Insurance Marketplace, also known as the Affordable Insurance Exchanges, will begin operating. The Department of Health and Human Services (HHS) is the lead agency on defining the structure and operations of the Marketplace. Open enrollment for insurance purchased through the Marketplace will start October 1, 2013, with coverage beginning as soon as January 1, 2014.

Starting in 2014, individuals who do not have access to affordable employer-sponsored insurance or other minimum essential coverage may be eligible to receive advance premium tax credits, paid directly to the insurer, for private insurance that they purchase through the Marketplace. Treasury and the IRS have provided guidance on how these tax credits work and can help reduce the cost of this coverage directly for the consumer, and HHS has provided guidance on how to apply for advance payments at the Marketplace. Under the ACA, the Marketplace will request tax return information from the IRS to determine eligibility for financial assistance such as premium tax credits. IRS staff have been working closely with HHS and the states on developing secure and efficient systems for the flow of this information.

Taxpayers who qualify for advance payments of the credit will reconcile these payments on their 2014 tax returns filed in 2015. Upon filing tax returns, these taxpayers will know the actual credit they qualify for based on their 2014 income. If the actual credit is larger than the sum of advance payments a taxpayer receives during the year, the taxpayer will be entitled to additional credit. If the actual credit is smaller than the sum of the advance payments, the taxpayer will owe the difference, subject to certain repayment caps included in the ACA, as amended.

Because the provisions mentioned above are substantial and require advance preparation, the IRS has established enterprise-wide governance and planning processes, coordinating efforts among

our business operations, information technology function, legal counsel and our Office of Safeguards. These planning efforts have had the benefit of independent reviews by both the Government Accountability Office and the Treasury Inspector General for Tax Administration.

Our budget requests in recent years reflect the need to invest in information technology (IT) systems to generally update our tax systems as well as administer the premium tax credit and other tax law provisions of the ACA. Of the funding requested in our FY 2012 and FY 2013 budgets related to ACA tax law implementation, 82 percent and 92 percent, respectively, was in our Operations Support account, which funds our IT and operations investments; almost 70 percent of the 2014 budget we requested for ACA tax law implementation would be used to continue the necessary IT development as the ACA is rolled out.

### **Supporting the Health Insurance Marketplaces**

Let me describe for you in more detail the supporting role that the IRS will play in the operation of the Health Insurance Marketplaces, or Exchanges.

When an individual seeks to purchase insurance through a Marketplace and seeks financial assistance, the Marketplace must determine what assistance, if any, the applicant may qualify for, such as Medicaid or the premium tax credit. To make that determination, the Marketplace will request federal taxpayer data. Upon request from the Marketplace, the IRS will provide, for each applicant, limited tax data<sup>1</sup> from the applicant's most recently filed federal income tax return. State Medicaid and the Children's Health Insurance Program agencies may also choose to request the tax data for their eligibility determinations.

It is important to understand exactly how this information will be transferred from the IRS to the Marketplace. The ACA designates the Department of Health and Human Services (HHS) as the conduit for information being shared with the Marketplace. The taxpayer data supplied by the IRS will be transmitted over secure, encrypted channels to the HHS Federal Data Services Hub, which was developed to facilitate these data transfers. The Federal Data Services Hub will not be storing taxpayer information, but merely routing that information to authorized users. The Marketplace, which requests and receives each data packet through the HHS data hub, will use the available tax data, together with data from other third parties and the applicant, to determine the best prediction of the applicant's 2014 income to be used to compute the assistance, if any, the applicant qualifies for. At no time is the tax data to be displayed to anyone outside of the Marketplace.

It is important to note that our ability to share tax return data with the Marketplace, via the hub, is being developed through new systems and services that our IT division has been creating. We are on target to have these new systems ready for deployment when open enrollment in the

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<sup>1</sup> The Marketplace request contains, for each person on the application, name, SSN, and relationship to the tax filer. This enables IRS to correctly locate and associate the limited relevant data from return records. The IRS returns information authorized under section 6103(1)(21), including limited income data from the face of the return, family size and filing status. The Marketplace will use this tax information, together with data from other sources, to make its determination about predicted 2014 income and eligibility for various programs.

Marketplace begins on October 1. Our IT project teams completed systems development, as well as interagency testing with HHS and the Center for Medicare and Medicaid Services (CMS), in June. Performance testing of these systems will continue through the summer.

Separate from the process of providing limited tax return data to the Marketplace, the IRS also is responsible for providing a computational service if the Marketplace determines that the applicant is eligible for, and interested in, advance payments of the premium tax credit. After the Marketplace has determined a predicted 2014 income figure, and without identifying the applicant, the Marketplace will submit a few data elements – such as a Marketplace-determined income figure and family size, and the Marketplace benchmark plan premium – for the IRS’ computational service through the HHS data hub, and receive back a single figure: the maximum advance premium tax credit resulting from those data inputs. Nothing in this computational process identifies individuals or contains tax data. The IRS merely provides a mathematical service, which supports consistent math at enrollment and on the later tax return, regardless of whether the inputs change.

### **Enforcing Proper Payments of the Premium Tax Credit**

While the focus for October 2013 is on preparing for the Marketplaces to begin operating, the IRS has also been preparing for the 2015 tax filing season. Beginning with 2014 tax returns filed in 2015, individuals will be eligible to claim the credit and will be required to reconcile any advances already paid to their insurance company on their behalf. The IRS will be required to promptly process accurate returns while also efficiently identifying and stopping any erroneous claims for the credit.

To facilitate this process, the Marketplaces will be transmitting over secure, encrypted channels to the IRS enrollment information for individuals purchasing coverage through those Marketplaces. This transactional information will include the fact and cost of coverage, and information on any advance payments of the premium tax credit made during the coverage year to the taxpayer’s insurance company on their behalf. While certain identifying information, such as name and SSN, is required to support the tax return processing, no personal health information is ever provided. The IRS will reconcile the information with what the individuals report on their tax returns so that the IRS can verify whether they received the proper amount of credit, are owed more, or must repay any excess advance payments. This information will help the IRS speed processing of returns and spot erroneous claims of the credit.

It is important to note that the IRS already routinely receives third-party information that helps it verify the accuracy of tax returns, and we have longstanding policies in place related to the safety and privacy of this information. We will use this experience to guide us in making sure that any taxpayer information we receive is properly safeguarded.

In addition to the data, tools and systems that the IRS uses to combat tax fraud of all kinds, we have some particular tools for enforcing proper payments of the premium tax credit. As mentioned above, the Marketplaces will be providing the IRS with key 2014 transactional data prior to the beginning of the 2015 tax filing season. Having this pre-positioned transactional data will allow the IRS to efficiently sort for many of the basic qualification and computational

elements of the premium tax credit. While the IRS does not share publicly all of the tools and techniques used for detecting non-compliance, it is important to note that as the tax returns are processed, for example, the IRS will be able to determine whether:

- There is a record of anyone on the return having enrolled at a Marketplace (a basic requirement to claim the credit);
- The return passes a basic check against a Marketplace record, but does not acknowledge that advance payments have already been paid directly to the insurance company and need to be netted against the credit calculation before a refund can be due; and
- The return reports inaccurately high premium costs or inaccurately low advance payments as compared to the Marketplace data.

Of course, additional eligibility and accuracy issues will also be checked using other ACA-specific information and by applying the same new and enhanced techniques we apply to all returns to detect non-compliance.

### **Protecting Safety and Privacy of Data**

Let me now turn to the steps that the IRS is taking to ensure the safety and security of the data being shared under the ACA. The information sharing to be done under the ACA comes against the backdrop of very strong taxpayer confidentiality protections as specified in the tax laws. In general, section 6103 of the Internal Revenue Code prohibits the IRS from sharing tax return data with anyone outside the agency.

Over the years, however, Congress has created a series of narrow exceptions to the restrictions in section 6103. Those exceptions allow the IRS to share taxpayer information for specific purposes and with proper safeguards. For example, the IRS is permitted to disclose tax return information to other federal agencies and state tax authorities to facilitate efficient tax administration. The ACA provides a specific exception to section 6103 for information sharing activities that the IRS will perform under the statute.

The IRS is already well positioned to provide the needed safeguards, given the longstanding experience it has in overseeing the transmission of data to federal and state agencies under previously enacted exceptions to section 6103. Agencies receiving return information from the IRS must meet significant safeguarding requirements, including strict recordkeeping and proper handling, storage and disposal of tax records.

The IRS Office of Safeguards has the responsibility for monitoring the nearly 300 federal and state agencies that currently are permitted to receive tax return data to ensure they are complying with all requirements. IRS Publication 1075, *Tax Information Security Guidelines for Federal, States and Local Agencies*, provides detailed background and procedures for data recipients.

In regard to upcoming data sharing under the ACA, the IRS has been collaborating with the other federal and state agencies involved in ACA implementation on the various processes and written agreements that are necessary for safeguarding personal information, including tax return data. We meet on a regular basis with every state and federal government entity that might receive

taxpayer data, to provide them with outreach and education, one-on-one consultations, and technical assistance on IRS data security requirements.

Among our collaborative efforts, the IRS and HHS have entered into a Computer Matching Agreement to meet the requirements of the Computer Matching and Privacy Protection Act. This agreement details the operations of the data exchange, as well as various disclosure restrictions and other requirements. The IRS and CMS have entered into an Information Exchange Agreement covering the use of HHS systems by the Marketplaces to transmit monthly and annual information reports to the IRS, and also covering use of the Premium Tax Credit Computation Engine by the Marketplaces. The IRS and CMS also have an Interconnection Security Agreement covering the security of the connection between the agencies. Because HHS is the conduit for the tax return information, it will in turn enter into similar agreements with all entities receiving the return information.

The IRS holds the Marketplaces and state agencies seeking tax return data under the ACA to significant data protection requirements. Before one of these entities can obtain tax return information, it must submit a Safeguard Procedures Report (SPR) to the IRS, and the IRS must approve it. This report details the steps that the entity has established or plans to take to protect the confidentiality of the tax records it will be handling. If any entities fail to establish adequate safeguards, taxpayer data will be withheld from them. Going forward, we will work with HHS and all other entities involved to ensure adequate data safeguards are in place, and we will provide ongoing oversight to ensure that all entities involved in data sharing continue to meet the safeguarding requirements.

## **Conclusion**

Chairman Camp, Ranking Member Levin, and members of the Committee, thank you again for the opportunity to testify on the steps we are taking to support the new Marketplace system, to protect and safeguard federal tax information, and to leverage new anti-fraud capabilities associated with the premium tax credit. We are taking all necessary steps to ensure that tax return information that flows to the Marketplace and state agencies carrying out the provisions of the ACA is secure and properly safeguarded. This concludes my testimony. I would be happy to take your questions.